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CHARLES ELMORE

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1946

No. 325

A. P. HUDSON and ISAIAH SMITH, SPECIAL RECEIVERS, ETC., ET AL, Petitioners,

vs.

H. E. GRANT, ET AL,
Respondents.

BRIEF FOR THE RESPONDENTS

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BRIEF FOR THE RESPONDENTS

Petition for Writ of Certiorari to the Supreme Court of the State of Tennessee, December Term 1945—Opinion not published—(Contained in the Record at page 135; Opinions on Petitions to Rehear, contained in the Record at pp. 161, 180.)

STATEMENT OF THE CASE

In order to avoid any possible confusion as to the facts of this case, we feel that it is necessary to restate the case, because petitioners' statement is not a fair or accurate one.

This is a general creditors bill brought by L. H. Brooks, Frederick Leake, and A. L. Goldberg for themselves and other Tennessee holders of investment contracts of the Fidelity Assurance Association, to impound certain securities deposited by it with James M. McCormick, Commissioner of Insurance and Banking of Tennessee, and to distribute the proceeds ratably among such holders. (R. p. 1)

The Fidelity, a West Virginia corporation, had been selling its investment contracts in that state and in most of the other states of the Union. Pursuant to the laws of West Virginia, it had deposited securities equal to its cash liability with the State Treasurer to be held by him in trust for its contract holders in West Virginia and in other states which did not require such deposit. Most of them did not require such a deposit; but some 15 of them, including Tennessee, did, the statute of Tennessee making this requirement being Tennessee Code section 6057 as amended by chapter 209, Acts of 1939.

Finding the Fidelity insolvent, the West Virginia Commissioner of Insurance caused a proceeding to be instituted April 11, 1941 in the Circuit Court of Kanawha County for a receiver and to wind up the Fidelity. That court appointed a receiver. Similar proceedings were brought in many other state courts, the present suit being filed April 21, 1941. In this cause the Chancellor entered a decree April 24, 1941 adjudging that the securities deposited with the Commissioner were "impressed with a trust or lien in favor of all the holders of investment contracts of defendant corpora-

tion sold in Tennessee," and sustaining the bill as a general creditors bill for all such holders who should claim the benefit of the deposit. (R. pp. 23, 24)

Soon after these suits in the state courts were begun, the Fidelity sought to enjoin and supercede them by filing in the Federal District Court for Southern West Virginia a reorganization petition under chapter X of the Bankruptcy Act. The Circuit Court of Appeals, however, dismissed that petition, and the Supreme Court affirmed the dismissal, leaving the state courts free to apply the deposited securities according to the respective laws of such states. (Fidelity Assurance Association v. Sims, 318 U. S. 608, 87 L. ed. 1032)

Thereafter, the West Virginia receivers appeared in the present suit and answered the bill. (R. p. 19) The securities deposited with the Tennessee Insurance Commissioner and held by the State Treasurer (ch. 157, Acts of 1941) were turned over to the Clerk and Master as Special Commissioner and sold by him, the proceeds approximating $236,000.00. There were several references to and reports by him as to contract holders who had filed claims to share in the fund. According to a list furnished by the Fidelity, there were some 600 contract holders in Tennessee, counting some who had purchased contracts elsewhere and moved here, and not counting others who had purchased contracts here and moved to other states. There were about 508 claims filed totaling a little over $260,000.00, this being the full amount these claimants had paid the Fidelity on their contracts. (R. p. 46)

While there were several different forms of these contracts, in all, but a few paid up in advance, the holder agreed to pay monthly payments for some 10½ years and the Fidelity agreed at the end of that time to pay the face amount to him in a stated number of equal annuities, or to pay a less amount in a lump sum. The Fidelity also agreed to set aside and maintain as a reserve, and to deposit in trust as required

by the laws of West Virginia, such sum as, together with interest thereon compounded semi-annually at the rate of 4½% per annum, would at any and all times equal Fidelity's cash liability on the contract and be sufficient to discharge the contract according to its terms. After as much as 12 monthly payments had been made by the holder on his contract, it had a cash surrender value, which at first was much less than the sum of such payments and increased proportionally until in eight or nine years it equalled that sum and thereafter exceeded it. If a holder defaulted in his monthly payments, he could keep his contract in force by paying up the past-due payments with 6% interest thereon at any time within a year after such default began; if his default extended for more than a year his contract ceased to be in force; but at any time within ten years from his first monthly payment he had the privilege of having a new contract issued to him upon paying the current monthly payment, a certain re-issue fee, and 1/10 of the first three past-due monthly payments, such new contract being credited with his previous payments and maturing later than the prior contract by a period equal to the period of his delinquency. (R. pp. 10, 11, 12, 13, 14, 15)

Under these provisions, on April 11, 1941, the date of Fidelity's insolvency, the contract holders consisted roughly of these three classes: (1) Those whose contracts were in force and had a cash surrender value because they had paid 12 monthly payments or more. (2) Those whose contracts were in force but had no cash surrender value because they had not paid as much as 12 monthly payments. This class was carried as "current" by the Fidelity until they were in default for as much as a year. (R. pp. 16, 17) (3) Those whose contracts were not in force because they had not paid as much as 12 monthly payments and had been in default for more than a year. Within ten years from the first monthly payment, they had the privilege of obtaining a new contract, credited with their

prior payments and re-dated to correspond with the period of delinquency, by making the required payments. (R. pp. 10 to 15)

The West Virginia receivers and complainants contended that the fund should be distributed on the basis of the surrender values of the contracts and paid pro rata to claimants of class (1), to the exclusion of the other two classes. The Chancellor reached this conclusion in an opinion filed December 9, 1943. (R. p. 52) Accordingly, on December 10, 1943, he entered a decree that the fund, after paying the expenses of administration, should be distributed among class (1) contract holders on the basis of the surrender values of their contracts; that such holders who had purchased their contracts in Tennessee but had become non-residents on April 11, 1941 should not share; that those who had purchased contracts elsewhere but had become residents of Tennessee on that date should share, their shares being reduced by any amounts recoverable by them from deposits elsewhere; and that the master should report the claimants and the respective amounts to be paid them, according to the principle of distribution fixed by the decree. (R. p. 50)

Following this principle, the master on January 29, 1944, reported a list of 412 claimants holding contracts with cash surrender value, and set out the amounts of such values, which aggregated approximately $185,000.00. One of class (2) claimants thus excluded was H. E. Grant, who had purchased two contracts in Tennessee, was a resident of that state April 11, 1941, and had paid on each of such contracts seven monthly payments of $15.00 each, or $210.00, both of such contracts being current. (R. pp. 16, 17) He excepted to the master's report upon the grounds that the cash surrender value was not the proper basis of distribution and that he should be allowed to share in the fund upon the basis of the amount paid by him on his contracts. (R. pp. 65, 67, 68)

The Chancellor entered a decree March 1, 1944, overruling Grant's exception, confirming the Master's report with certain modifications not here material, and directing the Clerk and Master as Special Commissioner out of the funds to pay (a) all the costs and his compensation of $2,000.00, (b) fees to solicitors of complainants in the sum of $26,000.00 plus $6,500.00 theretofore paid them, and (c) a partial dividend of 90% of the cash surrender values of their contracts to the claimants of class (1). (R. p. 71)

Grant appealed and insisted in the Court of Appeals that, under Code section 6057, as amended by chapter 209 of the Acts of 1939, Fidelity's deposit with the Commissioner was for the benefit of all its contract holders who purchased contracts in Tennessee, both those of class (1) and class (2): that the deposit constituted a trust whose beneficiaries were both classes of contract holders; and that the fund should be distributed pro rata to all of such holders on the basis of the amounts paid by them or the cash surrender values, whichever happend to be greater.

The insistences of Grant were sustained by the Court of Appeals, (R. p. 98) and, upon certiorari to the Supreme Court of Tennessee, that court, likewise, approved the insistences of Grant and affirmed the Court of Appeals. (R. pp. 135, 180)

SUMMARY OF ARGUMENT

(1) Petitioners contend (a) that H. E. Grant was not a party to the proceeding; and (b) that after the statutory time for appeal had passed, the appellate courts of Tennessee entertained his appeal and determined the rights of other parties to the proceedings.

A

H. E. Grant was a party to the proceedings in the Chancery Court of Davidson County, Tennessee, and

appeared, by counsel, in that court on numerous occasions when hearings were had, and he also filed proofs of claim (R. p. 41) and exceptions to the reports and decrees. H. E. Grant was a proper party because he was a contract holder of Fidelity, and, as such, a defendant in the general creditors suit.

B

The statutory time for appeal from the decree of the Chancellor had not passed at the time H. E. Grant excepted to the Chancellor's decree and prayed an appeal. Equity causes in Tennessee are not reviewed piece-meal, but upon a re-examination of the whole matter of law and fact appearing in the record (Tennessee Code sec. 9036). The right to appeal exists only after a final decree. Before the entry of a final decree there can be no appellate review of any interlocutory decree, save in exceptional cases.

The decree of December 10, 1943 was an interlocutory decree, as held by the Chancery Court of Davidson County, Tennessee (R. p. 71); the Court of Appeals of Tennessee, (R. p. 103); and by the Supreme Court of Tennessee (R. p. 136).

(2) Petitioners next insist that appellate courts of Tennessee, upon the appeal of one creditor on his own behalf, set aside judgments in favor of other parties to the suit, which judgments were res judicata and unappealed from, and thus deprived these judgment creditors of their property, without due process of law. The Tennessee law is well settled that, in cases—such as the present one, (general creditors suits) where the proper decree on appeal will necessarily affect the rights of the parties who have not appealed—the appellate court, although only one party has appealed, will determine the whole cause as it stood below before any decree was rendered. (Wood v. Cooper, 49 (2 Heisk) Tenn., 441, 445; Turley vs. Turley, 85 Tenn., 251, 259; State, ex rel, vs. Bolt, 130 Tenn., 212, 217, 218; Riley v. Shumate, 176 Tenn., 436)

The appeal by Grant under the applicable Tennessee law carried with it the review of the entire proceeding in the court below.

(3) The third insistence of the petitioners is but a re-statement of the second complaint—that they were unconstitutionally deprived of their property without due process of law by the setting aside of what they term '*res adjudicata*' judgments. This insistence is answered by the answer to the second insistence. There were no *res judicata* judgments as all steps taken in the chancery court were interlocutory and subject to review by the appellate courts of Tennessee; thus no constitutional question could arise here.

(4) The fourth insistence of the petitioners involves purely a matter of State law, because it involves the construction of a Tennessee statute under which the original deposit was made; and, as pointed out by this court, in the case of *Fidelity Assurance Association, et al*, vs. *Sims*, et al, 318 U. S., 605, 619," . . . state law must govern the distribution of the respective deposits; . . ."

(5) The fifth insistence of the petitioners is answered by the statement made with reference to the fourth insistence.—This is a matter of state law, and the deposit funds were deposited for the benefit of Tennessee creditors.

RESPONDENTS' INSISTENCE

(1) Respondents insist that there is no final decree in the Supreme Court of Tennessee which may be reviewed by this Court at this time.

The Supreme Court of Tennessee stated in its last opinion:

". . . We have remanded the cause to the chancery court of Davidson County. We have stayed proceedings there pending our further in-

vestigation of the petitions and motions we have just mentioned. The case will now be proceeded with in the chancery court in a manner not inconsistent with our original opinion, ignoring the opinion on the first petitions to rehear.

"If the parties hereto have rights not asserted on the record and the appeal before us, these rights must be developed in other litigation or by petitions filed in the court below. Whether they have such other rights, or whether such rights are now available to them, are questions that this Court obviously cannot determine upon this appeal.

". . . we are not sure that this cause can be said to have been finally determined."

[R. p. 182]

(2) The second proposition of the respondents is that there is no federal question. The Supreme Court of Tennessee speaking on this subject, stated:

"This stay is recalled, for on further consideration of the record sent up to us, it does not appear that any federal question was raised."

[R. p. 182]

Petitioners, in the Supreme Court of Tennessee, stated in their brief:

"There is only one real substantive question in issue, and that is whether the trust fund deposited by Fidelity in Tennessee shall be distributed (among Tennessee holders of investment contracts) upon the 'cash surrender value' basis, as decreed by the chancellor . . . , or whether distribution shall be upon 'amount paid in theory,' as held by the Court of Appeals."

[R. p. 136]

No claim of rights protected by the federal constitution was presented. The "alleged" federal question was first raised in the petition to rehear filed in the Supreme Court of Tennessee.

The Assignments of Error made by respondents in the Supreme Court of Tennessee make no mention of a claimed federal question. The respondents assigned four errors in the Supreme Court of Tennessee (R. pp. 131, 133): 1st. That the Court of Appeals had incorrectly construed the Tennessee statute—2nd. That the Court of Appeals had erroneously held that the Chancellor's decree was interlocutory. 3rd. That the Court of Appeals had erred in striking an affidavit filed for the first time in that court, which affidavit sought to supplement and change the record in that court. 4th. That the Court of Appeals was in error upon general state grounds for reversing the Chancellor's decree. No mention of any constitutional provision was made and no claim of federal right, privilege or immunity was asserted.

ARGUMENT

The respondents contend that, considering the case either upon broad and substantial grounds or upon a narrow, legalistic basis, (a) no substantial federal question is involved, and (b) no final decree exists in the case which can be reviewed at this time.

NO SUBSTANTIAL FEDERAL QUESTION

The Tennessee Deposit Statute

(a) The deposit statute of Tennessee required a deposit of securities at no time less than 100% of the issuers cash or contract liabilities, and a minimum of $10,000.00. The amendment to the Tennessee Code section 6057, effected by the Public Acts of 1939, was to strengthen the Blue Sky Law of Tennessee and to control investment companies in the sales of

securities in Tennessee. The Blue Sky Law as amended states, unequivocally, that the deposit is to be held for the benefit of contract holders, and that the deposit shall not be released until all liabilities to all contract holders are satisfied in full. (See statute set out in the opinion of the Court of Appeals. R. pp. 107, 108)

No mention is made in the statute of satisfaction of the liability of cash surrender value of contract holders, or satisfaction only to the extent of cash surrender value. The purpose of the Act is clearly expressed as being for the protection of all who purchased the contracts in Tennessee. The Blue Sky law had been construed by the Supreme Court of Tennessee prior to the amendment of 1939, and its purpose had been declared to be the protection of Tennessee investors. When the Supreme Court of Tennessee decided the present case, it merely reaffirmed its previous holding with reference to the meaning of the Blue Sky law. (Goodyear v. Meux, 143 Tenn. 287)

The present petitioners were the successful petitioners in the case of Fidelity Assurance Association, et al, vs. Sims, supra; and it was their insistence in that case that federal jurisdiction should be defeated so that each state could construe its own deposit statute, and apply the securities held by it to the satisfaction of its own contract holders. This Court in its decision sustained the insistence of the petitioners, holding, inter alia, "*Rights against local deposits will be adjudicated by the courts of the states nearer the homes of the beneficiaries and at a minimum of inconvenience, delay and expense. All the advantages of bringing all these funds to the district court for administration in conformity to diverse state law, and compelling claimants to go there and assert their rights, are not apparent.*"

The question submitted upon the instant record to this court is one of state law, to-wit, what is the correct

meaning of the Tennessee deposit statute? No federal question is presented, and the only question presented is the interpretation of the Tennessee statute, which is the exclusive province of the Supreme Court of Tennessee.

At the time this case was presented to the Court of Appeals and the Supreme Court of Tennessee, only one appellate court had passed upon the question. The United States Circuit Court of Appeals for the Eighth Circuit had decided the identical question and its holding was followed by the Tennessee appellate courts. (*In re Bankers Mortgage Company, 83 Fed. (2d) 550*). At the present time the only appellate courts which have passed upon this question are the Tennessee courts and the Eighth Circuit Court of Appeals.

NO FINAL DECREE

(b) Petitioners' attempt to show that there is, at present, a final decree in this case fails to come off. The status of the case at present is simply that it was remanded to the Chancery Court by the Supreme Court of Tennessee to be proceeded with in a manner not inconsistent with the opinion of the Supreme Court. The Supreme Court expressly recognized further litigation would develop and that, if parties were dissatisfied with the Chancellor's decision upon it, they might appeal. The opinion of the Court states:

> ". . . We have remanded the cause to the chancery court of Davidson County. We have stayed proceedings there pending our further investigation of the petitions and motions we have just mentioned. The case will now be proceeded with in the chancery court in a manner not inconsistent with our original opinion, ignoring the opinion on the first petitions to rehear.
>
> "If the parties hereto have rights not asserted on the record and the appeal before us, these rights

must be developed in other litigation or by petitions filed in the court below. Whether they have such other rights, or whether such rights are now available to them, are questions that this Court obviously cannot determine upon this appeal.

. . .

". . . we are not sure that this cause can be said to have been finally determined."
(R. p. 182)

JURISDICTION OF THE SUPREME COURT OF THE UNITED STATES

In cases such as the present one, before the jurisdiction of this court may be invoked, three things are essential: A final decree in the State court—a substantial federal question—the federal question must have been asserted in proper season and have been determined adversely to petitioners.

It is, perhaps, needless to cite authorities to the effect that this court will exercise jurisdiction only to review the final judgments, orders and decrees of State courts, because the statute with reference to the appellate jurisdiction of decrees of State courts, states: "(a) *A final judgment or decree in any suit in the highest court of a State . . .*" (*U. S. C. A., Title 28, Sec. 344* [a])

This Court has spoken on this subject many times, and has always embarked upon its investigation of the appeal or petition for the writ of certiorari by first satisfying itself that a final judgment exists.

This Court has many times said that nothing is better settled than that it is too late to raise a federal question for the first time in a petition for rehearing after the final judgment of the state court of last resort. (Susquehana Boom Co. v. West Branch Boom Co. [Pa. 1884], 110 U. S., 57) There is an exception to

this rule, however, if the state court actually entertains the petition and decides the federal question, and this appears upon the record, the statutory requirement that the right shall be specially set up and denied is held to be complied with. In the instant case, the federal right was claimed for the first time upon a petition to rehear in the Supreme Court of Tennessee, which was after the Court of Appeals of Tennessee had rendered its final opinion, and the Supreme Court of Tennessee had rendered its opinion. The Supreme Court of Tennessee did not entertain the petition and decide the federal question, but denied the petition and expressly stated that no federal question was presented upon the record before it. (R. p. 182). (St. Louis, etc. R. R. Co. vs. Shepherd [Okla. 1916], 240 U. S., 240.)

CONCLUSION

It is respondents insistence that the petition for certiorari should be denied; first, because there is no final decree to be reviewed; and secondly, because of the lack of any substantial federal question; and thirdly, because the alleged federal question was presented for the first time upon the petition to rehear in the court of last resort of Tennessee.

Respectfully submitted,

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CERTIFICATE OF SERVICE

Whitworth Stokes certifies that he served the foregoing Reply Brief upon counsel for Petitioners by mailing copies thereof to their proper address at Charleston, W. Va. This September 3, 1946.